



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Release Number: **201205013**

Release Date: 2/3/2012

Date: November 9, 2011

UIL Code: 501.36-01

504.00-00

513.04-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

This is our final determination that you do not qualify for exemption from federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Since you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

Letter 4038(CG) (11-2005)
Catalog Number 47632S

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

Date: September 21, 2011

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND:

B = state
C = date
D = church
E = denomination
F = denomination
G = denomination

UIL:

501.36-01
504.50.00
513.04-00

Dear

We have considered your application for recognition of exemption from federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

Issue

Do you qualify for exemption under section 501(c)(3) of the Code? No, for the reasons given below.

Facts

You were incorporated on C in the state of B. Your articles of incorporation state you are organized exclusively for religious purposes.

You indicate a close connection with D, an established G church with over 5000 congregants and over 100 churches nationwide. You have stated that you established a network with D to expand the distribution of materials. You indicate no further relationship with D in your Articles of Incorporation.

**Letter 4036(CG) (11-2005)
Catalog Number 47630W**

You have submitted Bylaws which govern your internal affairs. Subject to any limitations in the Articles of Incorporation or Bylaws relating to action requiring approval by the members or D, your temporal activities, business, and affairs shall be managed, and all corporate powers shall be exercised, by or under the direction of your board. The authorized number of directors shall be three. The qualifications of these directors are that they 1) must agree with D's statement of faith, 2) must have had a relationship with the church a period of 5 years minimum serving as a volunteer, employee, and/or contractor in any area with D, and 3) be familiar and understand the principles of D's vision and mission.

Your Bylaws indicate that you are not a subordinate to any religious entity, however, you follow the doctrine of the E church and D.

You distribute and sell religious products (books, music, CD's and other related items) through a customer sales network of churches and religious book stores throughout the United States. Customers are obtained through advertising that includes radio, magazines and the internet. You provided a sample of an advertisement which included select items for sales as well as your web site. You also submitted a catalog of all your materials available for sale including prices. Your website shows the items that are available for sale, lists various religious and musical tours, contains music video clips, audio files for download and photo galleries, and has a link for purchasing items.

The distribution of these products is achieved through sales on a wholesale level conducted by your employees who take the sales orders and ship the products. These product sales are directed to the F speaking religious population and are administered from your warehouse. Your facilities are leased from D.

Your products are distributed at the purchase price of the item sold plus an overhead factor. The overhead factor defrays administrative costs which include rent, payroll, insurance and office expenses. Your customers generally pay 25 percent to 30 percent less than market prices. Although you have stated that your sales are only to bookstores and churches, as sales to the general public would be at too high of a cost, products are available through ordering on your web site. Bookstores and churches who purchase your products then distribute them at retail to the public.

Your products are primarily purchased, but you do record some music and video tape worship services for DVD sales. This portion represents less than five percent (5%) of total sales. The proceeds from these sales help defray your operating expenses. Religious books and music are obtained from approximately 15 religious evangelical publishers. Products are purchased in volume to take advantage of discounts and maintain low costs.

Your products are generally not distributed free of charge but you will provide a one

time sample of music, DVD or book to an organization or individual at no cost. The free sample provides hands on experience of your product quality and mission to educate and attract new believers by providing messages through books, music (CDs) and instructive audio.

Your revenue consists solely of the sales of these products. Your main expenses include cost of sales for the purchase of product, contracted labor, commissions and advertising.

Law

Section 501 (c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable, educational and religious purposes.

Section 1.501 (c)(3)-1 (a)(1) of the Income Tax Regulations states that, in order to be exempt as an organization described in section 501 (c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501 (c)(3)-1 (c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501 (c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

In Revenue Ruling 60-351, 1960-2 C.B. 169, a corporation is organized and operated on a non-profit basis. It publishes a foreign language magazine containing fiction, poetry, book reviews and articles which it states is of a literary, scientific and educational character. The magazine is available to the general public through regular paid subscriptions. The corporation's income is derived mainly from subscriptions and sales of individual copies of the publication, and some is from advertising and contributions. Its expenditures consist of fees paid to authors for their works, salaries, printing, advertising, shipping packing, postage and other operating costs incurred in the publication of the magazine. It is devoted to publishing a magazine and selling it to the general public in accordance with ordinary commercial publishing practices. It is held that the corporation is not an exempt charitable, scientific, literary or educational organization within the meaning of section 501(c)(3) of the Code.

In Revenue Ruling 66-147, 1966-1 C.B. 137, an organization's specific purpose is to inform the interested public of current developments appearing in scientific and medical literature. The organization employs technical personnel who survey the world's medical and scientific publications as soon as they are published. They select and

abstract articles appearing in this literature. The abstracts are compiled in monthly publications and are distributed free of charge to anyone having particular interest in the subject matter. This organization qualifies for exemption from federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 179 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

In Fides Publishers Assn. v. United States, 263 F. Supp. 924 (1967) the government retroactively revoked the taxpayer's exempt status, concluding that, for the previous five years, the taxpayer was engaged primarily, if not solely, in publishing activities. The court noted that, to qualify for section 501(c)(3) exemption, the taxpayer must be "organized and operated exclusively for" an exempt purpose. The court rejected the taxpayer's argument that, rather than its primary activity, the court should focus on the end to which that activity was taken, namely, religious education. The court pointed out that the taxpayer's sole activity and purpose was the carrying on of the publishing trade and held that the taxpayer's purpose, rather than its goals, were the focus of section 501(c)(3).

B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352, 356-7 (1978), describes an organization whose sole activity was to provide consulting services for a fee to nonprofit organizations. It provided qualified persons to perform research projects for its clients. The fees charged by the organization were set at or close to cost but were not less than the organization's full cost of providing its service. The organization was denied exemption because it operated in a commercial, nonexempt manner. The provision of managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The Court held that the organization was not operated exclusively for charitable, educational or scientific purposes within the meaning of section 501 (c)(3) of the Code.

Application of Law

You are not operated exclusively for charitable, educational, or religious purposes consistent with Section 501(c)(3) of the Code nor Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations and therefore fail to meet the operational test. Specifically, the facts above indicate that you are not operated for exempt purposes but that you are operated in a commercial manner.

You are not described in section 1.501(c)(3)-1 (c)(1) of the regulations because more than an insubstantial part of your activities are devoted to non-exempt purposes. While you may indirectly advance religion in distributing your products, your primary concern

is the sale of religious publications. The purchase, sale, and distribution of religious products is not a charitable, educational or religious activity within the meaning of section 501 (c)(3) of the Code if done in a commercial manner. You provide a markup on products sold, advertise publicly to sell those products, and provide sales commissions which are all factors indicative of a commercial publishing operation. The sale of these materials, however religiously inspired, involves you directly in the conduct of a trade or business. You operate in a manner that is not distinguishable from a regular for profit publisher regarding the purchase, advertising, promotion and sales of your products. You have not demonstrated that the services you provide or fees charged for those services are offered in a noncommercial manner.

You are like the organization in Revenue Ruling 60-351, that publishes a foreign language magazine containing articles which it states are of a literary, scientific and educational character. The corporation's income was derived mainly from subscriptions and sales of individual copies of the publication, and some from advertising and contributions. Similar to this organization, you distribute and sell religious products (books, music, CD's and other related items) through a customer sales network of churches and religious book stores throughout the United States. Your income is derived from a markup on the cost of these items to cover expenses. The organization in this revenue ruling was held not to be an exempt organization within the meaning of section 501(c)(3) of the Code due to the publishing and selling of a magazine in accordance with ordinary commercial publishing practices. As seen in Revenue Ruling 66-147, the distribution of products free of charge differentiated that organization from operating as a commercial entity. Here, the sale and distribution of your products are in accordance with commercial distribution practices where a purchase is made, the merchandise is marked up and sold.

You are similar to the organization in Fides Publishers Assn. v. United States, which printed, published and sold products to promote religious culture. These products were sold at cost plus a markup. The organization argued that, rather than focusing on its primary activity, the court should focus on the end to which that activity was taken, namely, religious education. You have indicated your purpose to be advancing religion through the distribution of products. Much like the organization in this case you mark up and sell your products to generate enough revenue to cover operating costs which include salaries and commissions. The end result of your distributions may ultimately be religious education but your purpose is to purchase and distribute goods, not advance religion. For this reason your publishing activity is furthering a commercial rather than an exempt purpose under 501(c)(3) and you do not qualify.

You are similar to the organization in Better Business Bureau of Washington, D.C.. Inc. v. United States. 326 U.S. 179 in which the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes. Your activity of

administering the sales and distribution of religious products is substantial and is an activity that is primarily carried on for the purpose of conducting a commercial business. The purpose of this activity is not exempt under section 501(c)(3).

You are similar to the organization described in the B.S.W Group, which provided services to nonprofit organizations and was not exempt under section 501(c)(3). Your sole purpose is to administer the sale and distribution of religious products. You are dependent on the overhead markup that you charge to operate. The sale and distribution of religious products on a regular basis denotes the carrying on of a trade or business in a regular manner. Selling at cost lacks the donative element necessary to establish your activities as charitable versus commercial. Distributing religious products at cost plus markup is not sufficient to characterize the activity as religious. You do not qualify for exemption because you operate in a commercial manner rather than exclusively for charitable or religious purposes.

Applicant's Position

In order to further your exempt purpose, the communication of G beliefs and the word of God must include the distribution of religious resources that inspire and educate many congregations through distributors, bookstores and G churches where materials are sent to the different states across the nation. The faiths of all religions require nourishing through worship that is supplemented by books, worship, music and other inspirational products. In these difficult times, mankind can only improve through the nourishment of the human spirit through worship, and a continuing Christian education that uplifts and inspires. Your products provide this G education and inspiration through your books, bibles, music, and DVD's.

Service Response to Applicant's Position

The distribution of religious products, (books, bibles, music, and DVD's) can provide religious education and inspiration. However, the method by which these products are distributed must be reviewed in determining qualification under section 501(c)(3). Because of the commercial manner in which you distribute your products, as described in the preceding facts and analysis, you do not qualify for exemption under section 501(c)(3) of the Code.

Conclusion

Based on the information provided, you do not qualify for exemption under section 501(c)(3) of the Code. You are not organized and operated exclusively for charitable or religious purposes within the meaning of section 501(c)(3) of the Code because you operate in a commercial manner.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning.

You must submit the statement, signed by one of your officers, within 30 days from the date of this letter.

We will consider your statement and decide if that information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". These items include:

1. The organization's name, address, and employer identification number;
2. A statement that the organization wants to appeal the determination;
3. The date and symbols on the determination letter;
4. A statement of facts supporting the organization's position in any contested factual issue;
5. A statement outlining the law or other authority the organization is relying on; and
6. A statement as to whether a hearing is desired.

The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

The declaration must be signed by an officer or trustee of the organization who has personal knowledge of the facts.

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. To be represented during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice*

Before the IRS and Power of Attorney. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter to you. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure, Publication 892